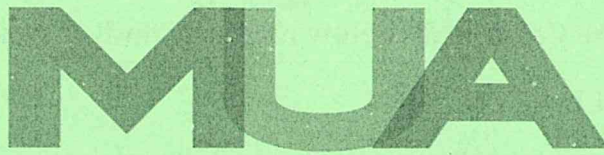


The
Management
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UNDERGRADUATE UNIVERSITY EXAMINATIONS
SCHOOL OF MANAGEMENT AND LEADERSHIP
DEGREE OF BACHELOR OF MANAGEMENT AND LEADERSHIP

BML 305 : AUDITING

DATE: 9TH DECEMBER 2016

DURATION: 2 HOURS

MAXIMUM MARKS: 70

INSTRUCTIONS:

1. Write your registration number on the answer booklet.
2. **DO NOT** write on this question paper.
3. This paper contains **SIX (6)** questions.
4. Question **ONE** is compulsory.
5. Answer any other **THREE** questions.
6. Question **ONE** carries **25 MARKS** and the rest carry **15 MARKS** each.
7. Write all your answers in the Examination answer booklet provided.

QUESTION ONE

Read the Case Study below carefully and, answer the questions that follow:

NEDS LIMITED

Neds is a small company which manufactures and sells high quality clothes. Its customers are mainly fashion boutiques. Neds had two directors, one of whom is non executive. The other is involved in day-to-day administration of the company. There are forty other employees, most of them working in the factory with two working in the warehouse, two in accounts and four being sales representatives. The Accounts staff are Jane and Sarah. Jane is responsible for processing sales and debtors whereas Sarah is in charge of purchases and wages and works on a part time basis; morning hours only.

Each of the sales representatives visit shops throughout the region; taking orders from customers which are recorded on a pre-numbered duplicate order form. Completed forms are passed to the Accounts department where Jane files one copy of the order form in numerical sequence and passes the other to the warehouse.

The completed order is dispatched from the warehouse by carrier accompanied by one copy of a dispatch note. The other copy is sent to Jane, who prepares an invoice based on the information it contains and on the company's price list. She sends one copy of the invoice to the customer and retains a second copy

Each Friday, Jane inputs the week's invoices into the computerized sales ledger then files the invoices alphabetically by customer name. Dispatch notes are not retained because filing space is limited.

Jane opens the post daily and lists remittances received from customers and every Friday she inputs the information listed to the sales ledger. Cheques received are banked daily by the executive director.

Jane reviews the sales ledger balances every month and writes to customers who have not paid within 90 days of receiving goods. The sales ledger is printed out annually for year-end purposes. Otherwise, no hard copy is printed and Jane reviews the sales ledger on the computer screen.

The company's computer package includes the facility to produce a sales day book and sales ledger control account. These are not used because Jane considers that the low volume of transactions (50-75 invoices per week) makes them unnecessary.

Required:

- a) State with reasons, what you consider to be potential weaknesses in Neds present system of accounting for sales and receivables (15marks)
- b) Describe controls that a small firm such as Neds could feasibly adopt to overcome the weaknesses you have identified (10marks)

QUESTION TWO

According to International Standard on Auditing (ISA) 230 *Audit documentation*, the auditor is required to document "evidence that the audit was planned and performed in accordance with ISAs and applicable legal and regulatory requirements"

Required:

Describe the working papers which would be of particular assistance to you as a newly appointed senior in charge of a recurring audit at the final audit stage (the previous senior having left the firm after the interim audit)

- a) In familiarizing yourself with the client company (7marks)
- b) When you are planning the current year's final audit (8marks)

QUESTION THREE

Your firm is the external auditor of Two way Distributors, a listed company. The company operates from a head office in Nairobi and has sales outlets and warehouses around the country. The directors have decided that the company has reached a size when it needs an internal audit department, As is becoming increasingly common, the directors have asked your firm to provide this service to the company as well as being the statutory auditor of the company's annual financial statements:

Required:

- a) Describe the matters you should consider and the action you will take to ensure your firm remains independent as external auditor of the annual financial statements (8marks)
- b) Describe the advantages and disadvantages to Two way Distributors of your firm providing an internal audit service (7marks)

QUESTION FOUR

The ISA 500- Audit evidence, requires that: "The auditor should obtain sufficient appropriate audit evidence to be able to draw reasonable conclusions on which to base the audit opinion"

- a) In relation to ISA 500 -Audit evidence, state the requirements of the standard and define Audit evidence and state what constitutes audit evidence (5marks)
- b) Briefly explain the stages in audit sampling (10marks)

QUESTION FIVE

- a) With reference to ISA 240, define the term error and state FOUR types of errors (5marks)
- b) Briefly explain how internal control systems can be used to detect frauds in an organization (10marks)

QUESTION SIX

- a) Briefly explain the factors which might affect the extent of use of analytical review in an audit engagement (10marks)
- b) In reference to auditing, define the term Vouching and explain when it is useful in auditing (5marks)